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SUBJECT: SENATOR SHELBY MEETS SPANISH ECONOMICS OFFICIALS

1. Summary: Senator Richard Shelby met separately in Madrid March 28 with two high-ranking Spanish government officials in the government, two ministries dealing with economic and finance issues. The Senator and his hosts discussed the current state of the Spanish economy, the impact of EU enlargement on Spain, the long-term impact of the EU, recent agreement to modify its stability pact, how Spain and the U.S. can remain competitive economically with China and India, and the relative costs of health care in Spain and the U.S. End summary.

2. Senator Richard Shelby met separately in Madrid March 28 with two high-ranking Spanish government officials in the economics and finance arenas: Miguel Angel Fernandez Ordonez, secretary of state for finance and budget in the Ministry of

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Economy and Finance, and Pedro Mejia Gomez, secretary of state for tourism and commerce in the Ministry of Industry, Tourism and Commerce. Senator Shelby was joined in both meetings by two Banking, Housing and Urban Affairs Committee staffers, Mrs. Shelby, embassy, economics counselor, poloff and military escort.

Fernandez: Stability Pact Least of All Evils

3. Fernandez opened the first meeting by discussing EU enlargement. He said Spain is facing challenges brought on by an enlarged market that includes countries with lower labor costs. In his view, though, this will be good for Spain and rest of the EU in the end, because open markets and economies are by their nature good. One clear disadvantage enlargement brings for Spain, however, relates to EU funds. In recent years more EU common funds went to Spain for infrastructure and other improvements than to any other EU member. Spain had been receiving about 1 percent of its GDP in EU funds. With enlargement, Spain will go from being a net recipient of funds to a net donor. Fernandez said Spain hopes to make the change gradually.

4. Senator Shelby asked Fernandez what the biggest challenge is facing the Spanish economy. Fernandez replied that it was not having its own currency to devalue to remain competitive. Instead, Spain is focusing on education, research and development and technology to increase productivity, which is the only way Spain can stay competitive. On the EU's new stability pact agreement, Fernandez thought the agreement reached was the least of all evils. In the end, the 3 percent figure is much lower than in other economies like the U.S. or Japan.

Mejia: EU Monetary Policy Not Designed for Spain

5. Mejia began his meeting with the Senator by explaining that the Spanish economy is affected by many of the same forces that impact the U.S. economy, including a substantial trade deficit. EU monetary policy, said Mejia, is currently designed for a country like Germany that has low domestic demand, not Spain, which has high domestic demand. Spiraling oil prices and a weak U.S. dollar resulted in a trade deficit in January 2005 that was 50 percent higher than the same month in 2004.

6. The Senator said that in the U.S. we have a high trade deficit and budget deficit, and have decided to attack the latter first by trying to live within our means. The U.S. economy overall is sound, however, and small and medium businesses are the growth engine in the U.S.

7. Mejia then commented that the Spanish government wants to increase exports from Spain to the U.S. Spain has put the U.S. at the top of a list of nine countries to target for increased exports. The environment for stable businesses in the U.S. is excellent right now, and Spain wants to take advantage.

8. The Senator asked Mejia what he thought of the stability

pact agreement. Mejia did not believe the agreement would have any long-term negative impact on the EU. In fact, it was probably a net positive because it showed the EU could deal with changing circumstances. On the whole, the EU is doing extremely well economically even given a variety of challenges like German reunification, and is much better off than most people would have predicted 20 years ago.

9. Both agreed that China and India will be major competitors for the U.S. and EU for many years to come. While neither Spain,s nor the U.S.,s labor market will be as flexible as China,s or India,s, the EU and U.S. can use their technological advantage to increase productivity, which in turn will help them counter China,s and India,s lower costs of labor.

10. Senator Shelby observed that 56 percent of the U.S.,s budget goes to public expenditures like Medicaid, and asked what the comparable number was for Spain. Mejia admitted he did not know, but explained that in Spain medical costs are much lower than in the U.S. because the state is the only purchaser of medical services. The government uses its purchasing power to get the best possible prices on medications and medical services for the citizens. The Senator commented that it is the lack of competition for medical services in the U.S. that has lead to the enormous cost of health care. Medical services in the U.S. are not subject to the laws of supply and demand.

11. Senator Shelby's staff has approved this message.

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